2000

The Geothermal Company, a Nevada Corporation v. Far West Capital, Inc, Utah Corporation; Steamboat Development Corporation, a Utah Corporation : Reply Brief

Utah Court of Appeals

Mary Anne Q. Wood; Kathryn Ogden Balmforth; Wood and Crapo LLC; Attorneys for Appellees.
David C. Wright; Kruse, Landa & Maycock, LLC; Attorneys for Appellant.

IN THE UTAH COURT OF APPEALS

----oo0oo----

The Geothermal Company, a Nevada Corporation,	)	
Appellant,	)	
vs.	)	
Far West Capital, Inc., a Utah Corporation; Steamboat Development Corporation, a Utah corporation,	)	Case No. 20000348
Appelles.	)	

APPELLANT'S REPLY BRIEF

An appeal from a final decision of the Third District Court.
Judge William B. Bohling

DAVID C. WRIGHT (5566)
KRUSE, LANDA & MAYCOCK, L.L.C.
Attorneys for Appellant
Eighth Floor, Bank One Tower
50 West Broadway
Salt Lake City, Utah 84145-0561
(801) 531-7090

Mary Anne Q. Wood
Wood & Crapo, LLC
60 East South Temple, Suite 500
Salt Lake City, UT 84111
Attorneys for Appellees
(801) 366-6060

IN THE UTAH COURT OF APPEALS

----oo0oo----

The Geothermal Company, a Nevada Corporation, Appellant, vs. Far West Capital, Inc., a Utah Corporation; Steamboat Development Corporation, a Utah corporation, Appelles.	)	Case No. 20000348

APPELLANT'S REPLY BRIEF

An appeal from a final decision of the Third District Court,
Judge William B. Bohling

DAVID C. WRIGHT (5566)
KRUSE, LANDA & MAYCOCK, L.L.C.
Attorneys for Appellant
Eighth Floor, Bank One Tower
50 West Broadway
Salt Lake City, Utah 84145-0561
(801) 531-7090

Mary Anne Q. Wood
Wood & Crapo, LLC
60 East South Temple, Suite 500
Salt Lake City, UT 84111
Attorneys for Appellees
(801) 366-6060

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

OTHER AUTHORITIES

RULES

ARGUMENT

I. FWC ARGUES FACTUAL MATTERS THAT ARE EITHER NOT SUPPORTED BY THE RECORD OR THAT ONLY POINT OUT THE FACTUAL DISPUTES IMPROPERLY RESOLVED ON ITS 12(b)(6) MOTION.

Geothermal's opening brief invited discussion of the standards and analysis of a 12(b)(6) motion, both at the trial level and on appeal. The invitation was declined, mostly. FWC does contend that neither the trial court nor this Court should invent facts sufficient to save an otherwise defective complaint. Geothermal, of course, does not contend otherwise. Invention is not required, but an assessment of what has been pled *and* what might be pled – "any set of facts" – is required. *Olson v. Park-Craig-Olson, Inc.*, 815 P.2d 1356, 1360 (Utah App. 1991).

Rule 12(b)(6) jurisprudence dictates and reason suggests that the earlier a claim is dismissed the more exacting is the standard that must be overcome to achieve dismissal and to protect that result on appeal. The opinions of this court and the Supreme Court routinely begin with a statement of the standard of review, and for a good reason. The standards are issue-driven. *State v. Pena*, 869 P.2d 932 (Utah 1994).

The rules of the analysis are categorical: there must be "certainty" that the plaintiff cannot recover under any facts that could be pled to support the claim. *Arrow Indus. v. Zions First Nat. Bank*, 767 P.2d 935, 936 (Utah 1998). That is muscular language. It is a standard unchanged since *Conley v. Gibson*, 355 U.S. 41 (1957): dismissal is improper "unless it appears *beyond doubt* that the plaintiff can prove no set of facts in support of his claim . . . ."(emphasis added).

It seems, however, that courts seem to still grapple with the tension between rule 12(b)(6) and rule 8(a). Rule 12(b)(6) "is the successor of the common law demurrer and the code motion to dismiss . . . ." 5A FEDERAL PRACTICE & PROCEDURE § 1349, at 190-91 (2d ed. 1990). Yet, rule 8(a), however, took the pleading process out of the rigid code pleading requirements. In *Blackham v. Snelgrove*, 280 P.2d 453, 455 (1955) the following was observed:

> Thus, it can very often be found stated in these cases that a complaint is required only to give the opposing party fair notice of the nature and basis or grounds of the claim and a general indication of the type of litigation involved.

In *Cheney v. Rucker*, 381 P.2d 86, 91 (1963), decided in the context of pleading affirmative defenses, the Court noted this about the real meaning behind notice pleading:

> [The rules] must all be looked to in the light of their even more fundamental purpose of liberalizing both pleading and procedure to the end that the parties are afforded the privilege of presenting whatever legitimate contentions they have pertaining to their dispute. *What they are entitled to is notice of the issues raised and an opportunity to meet them. When this is accomplished, that is all that is required.* Our rules provide for liberality to allow examination into and settlement of all issues bearing upon the other party safeguard the rights of the other party to have a reasonable time to meet a new issue if he so requests. (emphasis added).[1]

FWC avoids serious discussion of these rules. It instead argues the merits, invoking a factual analysis to support dismissal. Except for the purpose of culling inferences, a factual analysis has no place in a 12(b)(6) motion. The test is not whether the claims are any good, or whether the complaint is a model of clarity, but only "whether the petitioner has alleged enough in the complaint to state a cause of action." *Alvarez v. Galetka*, 933 P.2d 987, 989 (Utah 1997).

---

[1] That passage was quoted with approval in *Eie v. St. Benedict's Hospital*, 638 P.2d 1190, 1193-94 (1981) (answer referring generally to fraudulent inducement, estoppel and breach by plaintiffs was sufficient pleading to raise the issue that parties' agreement was not integrated and was therefore subject to modification by contemporaneous oral communications).

Under a notice pleading regime, the bar is set quite low. *Consolidated Realty Group v. Sizzling Platter, Inc.*, 930 P.2d 268, 275 (Utah App. 1996).

To affirm in this case is to announce a qualitatively higher standard of pleading and to remove established limitations on the trial bench when analyzing a 12(b)(6) motion. Issues of integration, ambiguity and reasonableness would be fair game at a stage far earlier in the trial court than has ever been allowed or that was contemplated when rule 8 was adopted. Deciding such issues—especially reasonableness—on summary judgment is fraught with difficulty. It is even more dangerous on the scant record available on a 12(b)(6) motion.

Both below and on appeal, FWC argued disputed facts to support dismissal.

FWC adopts a unique approach to protecting its 12(b)(6) dismissal on appeal. Whenever needed, facts, unsupported by any record citation, are inserted into the mix to support FWC's position—to in effect explain its thinking during the contract negotiations. That approach started in the trial court. FWC argued below that the agreement to reimburse the closing costs would not have made sense because "the operating statement states *implicitly* that [Geothermal doesn't] have any operating history . . . ." (Tr. 27)(emphasis added).

FWC complained below also that Geothermal did not have "any significant assets or sources of funds." *Id.* An "operating statement," whatever that is, was not part of the record. And what it states "implicitly" seems a strange way to support a 12(b)(6) motion. These were factual matters not even mentioned in the complaint, a fact that by itself renders them meaningless under a 12(b)(6) analysis.

FWC approaches this appeal the same way. Its statement of facts does not state facts so much as argue them. FWC begins its statement of facts by announcing that it was the "owner of a new, valuable, but temporarily cash-strapped geothermal energy plant . . . ." (FWC brief at 5). The only one of those facts supported by the record is that FWC was an owner (R. 16:004).

According to FWC, the agreement with Geothermal

> bristles with express provisions reflecting FWC's lack of certainty about [Geothermal's] ability to raise cash at all—let alone on favorable terms—and FWC's consequent need for the ability to terminate the transaction if the terms ultimately presented were unfavorable.

(FWC brief at 6).

This argument raises two interesting points. First, if this argument is directed at the overall transaction—the purchase of the 50% operating interest in the geothermal plants—then it is wasted effort. No plausible reading of paragraph 7 or any other provision of the agreement supports the notion that FWC could cancel because it was concerned about the overall financing. The only contingency was the anticipated loan, which started out at $1 million and ended up at $300,000. (R. 018-19; 029).

Second, because a loan was contemplated, the parties would have had to negotiate regarding security, interest rate, repayment terms, and other terms normally part of a loan. Such terms were initially spelled out in the August 10 agreement. (R.019). The parties *must* have anticipated different terms after the amount was reduced to $300,000 because the February 3 modification says that the loan terms were "yet to be created." (R.031).

This leads to another factual dispute created by FWC. It argued that it cancelled because of dissatisfaction with the loan terms (leaving aside for the moment whether it actually had any

loan terms to review). (R. 25). FWC seems now undecided about why it cancelled. It mentions on appeal that its geothermal plant was "temporarily cash-strapped," (FWC brief at 5), and that as negotiations continued, its plants "had survived without the quick infusion of cash" and that they were "more profitable and, hence, more valuable than it was thought to be . . . ." *Id.* at 15.

Recall that the complaint alleges that FWC cancelled, not because of some loan that was, according to FWC now, no longer needed, but because its price had gone up thanks to improved conditions at the plants. (R. 009). But cancellation for this reason—that FWC could do better—was not permitted, at least if FWC's argument that the agreement is unambiguous in this regard is accepted.

FWC's central theme on appeal is that it had an unqualified right to cancel if the loan was either not funded or was otherwise unacceptable. The loan was, according to FWC, "the linchpin of the entire transaction . . . ." (FWC brief at 15 and *passim*). There was, therefore, a factual dispute about just why FWC cancelled. FWC states at least twice in its brief that it cancelled the agreement "pursuant to its express terms." (FWC brief at 26, 27). Cancellation was limited expressly to the loan terms and nothing else, and certainly not the possibility that FWC might change its mind because its energy plants were performing better than expected.

II. FWC MISAPPLIES THE LAW CONCERNING THE IMPLIED TERM OF GOOD FAITH AND FAIR DEALING.

FWC argues for an exception to the implied good faith term inherent in this and every other contract. FWC contends that its right to cancel is unfettered by a good faith obligation

because the right is spelled out in the agreement and is therefore a risk "expressly assumed" by Geothermal. (FWC brief at 24).

This argument is merely a variation on an already rejected theme. If adopted, it would negate entirely the long-standing good faith obligation. In *Olympus Hills Shopping Ctr. v. Smith's Food & Drug Ctrs.*, 889 P.2d 445 (Utah App. 1994), *cert. denied*, 899 P.2d 1231 (Utah 1995), the issue was "whether parties who retain express power or discretion under a contract can exercise that power or discretion in such a way as to breach the covenant of good faith and fair dealing." *Id.* at 450. This Court said they can: "Our courts have determined that a party must exercise express rights awarded under a contract reasonably and in good faith." *Id.* (citations omitted).

Resource Management Co. v. Weston Ranch and Livestock Co., 706 P.2d 1028 (Utah 1985) is indistinguishable on a reasoned analysis. There, the operative agreement contained the following:

> It is agreed and understood by the parties that THE COMPANY may, at any time, in its sole discretion, terminate this Agreement in the event it determines there is not sufficient promise of minerals of commercial value on the subject properties covered by the Agreement, sufficient to justify the further expenditures of time or money by THE COMPANY.

Id. at 1034.

The broad right provided by this language was subject to the obligation of good faith and fair dealing. *Id.* at 1038 Conditions to cancellation come with an obligation to evaluate those conditions in good faith. Otherwise, as FWC argues, the inherent term of good faith is easily sidestepped by merely spelling out the cancellation right in the agreement. "Even if the promisor

is himself to be the judge of the cause or condition, he must use good faith and an honest judgment." *Resource Management*, 706 P.2d at 1038, *quoting* Corbin on Contracts § 165, at 86-87 (1963).[2]

Resource Management relied in part on *Richard Bruce & Co. v. J. Simpson & Co.*, 243 N.Y.S.2d 503 (1963). There, a party had the right to terminate at any time if prior to a date certain the party "in its absolute discretion[] shall determine that market conditions or the prospects of the public offering are such as to make it undesirable or inadvisable to make or continue the public offering [under the agreement]." *Resource Management,* 706 P.2d at 1037. Even language this broad was limited by the obligation of good faith and fair dealing. *Id.* Parties to an agreement should not be held to FWC's proposed rule – that a party assumes by such language the risk that *express conditions* can be ignored.

Here, cancellation was conditioned expressly on the acceptability of loan terms that everyone agreed would be presented in loan documents "yet to be created." (R. 59). As for the "business terms and conditions associated with the loan," no such terms and conditions could exist until the loan was actually proposed. Only then could FWC determine whether such terms and conditions were "unfavorable." (R. 59).[3]

---

[2] *Leigh Furniture and Carpet Co. v. Isom*, 657 P.2d 293 (Utah 1982) says the same thing. There, despite complete discretion, a corporation acted in bad faith when it refused to approve certain business partners without considering their merits.

[3] The risk argument urged by FWC is the crux of the holding in *Olympus Hills.* This Court observed as follows:

> Thus, in this case, our inquiry does not end with the recognition that Smith's had the discretionary power or contractual authority to operate "any lawful retail selling business." The question is whether, upon a motion for summary judgment or directed verdict, the trial court properly found that reasonable minds could differ as to whether Smith's wrongfully exercised

FWC attempts to negate the conditions expressed in paragraph 7 by proposing an entirely new one: that nothing was binding until the loan proceeds were actually received. (FWC brief at 23). That argument begs the initial question, as no loan proceeds could be received until the loan terms were presented, evaluated, even negotiated, and then agreed on. Indeed, FWC's chief contention is that it had the absolute right to evaluate those terms. Plainly it could not pocket the loan proceeds first and then decide whether to actually borrow them.[4]

The good faith and fair dealing obligation "is not susceptible to brightline definitions and tests." *Olympus Hills*, 809 P.2d at 450 n.6, (citation omitted). Conceptually, then, it seems that, short of some fact as "brightline" as a statute of limitations, resolving a fact-driven issue like good faith and fair dealing is extremely difficult at the pleading stage. The ultimate test of good faith, after all, is "reasonableness." *Id.* at 451-52 and n.7.

III. GEOTHERMAL HAS NOT ATTEMPTED TO REWRITE THE AGREEMENT, BUT INSTEAD TO ENFORCE IT ACCORDING TO ITS TERMS.

FWC argues that Geothermal's position is an attempt to retrofit the agreement with terms more beneficial than originally agreed. (FWC brief at 24). Geothermal argues nothing of the kind. Indeed, it is FWC that now seeks a better agreement than the one it made. Its position is

---

this power for a reason beyond the risks that Olympus Hills assumed in its lease with Smith's or for a reason inconsistent with Olympus Hills's "justified expectations." *See St. Benedict's*, 811 P.2d at 200; Restatement (Second) of Contracts § 205 cmt. a (1981).

Olympus Hills, 889 P.2d at 451.

[4] Even where the contract is not complete – as in an agreement to agree – the parties are bound by the implied term of good faith and fair dealing: "There is no reason why an enforceable agreement to agree does not give rise to the covenant of good faith and fair dealing." *Brown's Shoe Fit Co. v. Olch*, 955 P.2d 357, 366 (Utah App. 1998).

that it could cancel preemptively, before it even reviewed the loan terms in documents that did not exist. That must be its position because no loan documents were ever created and no loan was proposed and yet FWC claims to have cancelled because of dissatisfaction with the loan.

FWC contends that Geothermal asks this court to "read into the contract a right for [Geothermal] to make the unilateral determination to substitute a cash payment for the Loan . . . " (FWC brief at 24-25). That is not Geothermal's position. The fact is, "as a further *accommodation*, [Geothermal] *agreed* to reimburse" FWC up to $300,000. (R. 16:008)(emphasis added). It is no coincidence, of course, that this amount is the same as the loan amount in the agreement. (R. 16:031). "[L]egal and associated closing costs" were FWC's concern as the closing approached. (R. 16:008). These allegations do not suggest a "unilateral determination" by Geothermal; they suggest a negotiated agreement.

FWC contends further that Geothermal attempts to "bypass the process set out in the LoI which gave FWC rights to negotiate and be satisfied with the terms of the ultimate transaction and, absent such satisfaction, to walk away." (FWC brief at 25). No plausible reading of the agreement, and particularly paragraph 7 of the February 3 version (R. 16:031), supports such a right. FWC suggests with that language that it could cancel because it was not satisfied with the "ultimate transaction . . . ." Paragraph 7, however, plainly limits cancellation based on an assessment of the loan terms only.

In terms of enforceability, Geothermal is accused of arguing "several straw men," but with citation to only one. (FWC brief at 18, n.5). Geothermal does not argue the position FWC ascribes to it. That portion of Geothermal's brief, properly understood, addresses integration.

Paragraph 7's integration language is anything but aggressive. It says that there will be at least one more agreement – the loan – and that other modifications require board approval.

The factual question of integration alone casts severe doubt on the trial court's ruling. There is no straw man lurking in the argument that integration – an implicit finding in the ruling below – is a factual question resolved improperly on a 12(b)(6) motion.

IV. THE STATUTE OF FRAUDS DOES NOT APPLY BECAUSE OF THE IMMATERIAL MODIFICATION TO THE AGREEMENT.

FWC contends incorrectly that Geothermal seeks to impose a unilateral "substitute performance." (FWC brief at 25). There was indeed a substitute, but it was not unilateral. The claim is that, to "accommodat[e]" FWC, Geothermal "agreed" to pay a cash reimbursement instead of lending the $300,000. (R. 008). Why Geothermal would *unilaterally* alter the agreement to its own detriment—giving up the right to have its $300,000 repaid—is never explained.

Plainly, the reasonable inference never drawn by the trial court is that Geothermal "agreed" to this term because that's what FWC wanted. That this was an *agreed* term is the whole point. And this modification to the agreement offends neither the agreement nor the statute of frauds because the "*agreed*" change—reimbursement instead of a loan—is immaterial. Money—the same amount—was still changing hands; the only modification was whether it had to be paid back.

FWC contends that "[i]t cannot seriously be argued that the loan was immaterial to the transaction." (FWC brief at 21). Fortunately for the serious-minded no one argues that.

Materiality depends on the circumstances. FWC contends that circumstances changed, such that its plants no longer needed that "quick infusion of cash...." (FWC brief at 15). The amount of money to change hands never changed after the February 3 agreement – it was still $300,000. FWC was still getting these funds, but without having to borrow them. Does FWC seriously contend that, for the deal to close, it *must* borrow, and therefore repay, the money rather than accept free reimbursement?

If the statute of frauds were to play a role in this issue, it would surely cut the other way. That is, had Geothermal claimed the reverse of what actually happened—that a cash reimbursement was modified to be a loan instead—thus requiring repayment where no such obligation had existed before, then applying the statute of frauds would at least make sense. It would make sense for FWC to argue the statute to preserve the better deal. Here, the party to whose detriment the modification was intended is trying to enforce that modification. FWC needs no protection behind the statute of frauds.

V. GEOTHERMAL PLED SUFFICIENT FACTS AND THE ELEMENTS OF ITS CLAIMS TO SURVIVE A 12(b)(6) MOTION.

Ultimately, conflicting interpretations of contract terms and indecision about the basis for canceling do not drive the 12(b)(6) analysis. What does drive it is the uncomplicated question of whether enough facts have been pled to support the claims. *Mackay v. Cannon*, 996 P.2d 1081 (Utah App. 2000).

Geothermal pled two versions of breach of contract—one written and one oral. Paragraphs 25 through 33 of the complaint (R. 009-010) allege contracts, breach and damages.

Geothermal alleges its own performance. (R. 007). Geothermal pled the critical fact that FWC cancelled because it wanted more money because its plants were performing better. The agreement allows cancellation only in connection with the loan. For background allegations, the complaint is prolix. The same is true for the quantum meruit claim. Facts sufficient to show a benefit and its appreciation have been pled. (R. 012-013). *See Olson*, 815 P.2d at 1360 (1991) (elements of contract implied in law branch of quantum meruit).

Having pled a factual basis for its claims, Geothermal did enough to survive a 12(b)(6) motion because it complied with rule 8(a). The trial court erred by going beyond those allegations and construing the agreement, including necessarily factual issues of integration, ambiguity and good faith cancellation. Such claims are typically not resolved, or resolvable, as a matter of law. *See, e.g., Cook v. Zions First Nat'l Bank*, 919 P.2d 56, 61 (Utah Ct. App. 1996) ("whether there has been a breach of good faith and fair dealing is a factual issue, generally inappropriate for decision as a matter of law"); *Olympus Hills*, 889 P.2d at 458 ("Whether a party has materially breached a [contract] is generally a question of fact for the fact finder.").[5]

"The days of strict adherence to draconian formalities at the pleading stage are over." *Consolidated Realty Group,* 930 P.2d at 275. The pleadings are restricted to general notice-giving. *Williams v. State Farm Ins. Co.,* 656 P.2d 966, 970-71 (Utah 1982). If these statement

[5] As surprising as dismissal of these claims is, it is just as surprising that the trial court did not allow leave to amend. "[D]ismissal under Rule 12(b)(6) generally is not final or on the merits and the court normally will give plaintiff leave to file an amended complaint.... Amendment should be refused only if it appears to a certainty that plaintiff cannot state a claim." *Alvarez*, 933 P.2d at 991 (citations omitted). Geothermal's current counsel likely would have prepared the complaint differently, but prior counsel should have at least been afforded the opportunity of amending.

mean what they say, then at the pleading stage a trial court errs when, as happened here, it construes an agreement or decides issues of integration and good faith.

CONCLUSION

Disputed factual issues—integration and good faith conduct, to name just two—had to be resolved before the trial court could rule as it did. On a 12(b)(6) motion that is reversible error. There is no room to be wrong, as every doubt is resolved and every reasonable inference drawn in plaintiff's favor. Even now, FWC's position is inconsistent as it tries to decide just why it cancelled the agreement. This case was not ripe for summary judgment, let alone dismissal on the complaint. This Court should, therefore, reverse.

DATED this 19th day of December, 2000

Respectfully submitted,

KRUSE, LANDA & MAYCOCK, L.L.C.

DAVID C. WRIGHT (5566)
Attorneys for The Geothermal Company

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing **APPELLANT'S REPLY BRIEF** was hand delivered to the following this 19th day of December, 2000.

Mary Ann Q. Wood
WOOD CRAPO, L.L.C.
500 Eagle Gate Tower
60 East South Temple
Salt Lake City, UT 84111